Supreme Court, U.S.
FILED
AUG 18 1995
CLERK

No. 95-128

In The

Supreme Court of the United States

October Term, 1995

UNITED STATES OF AMERICA,

Petitioner,

v.

COUNTY OF SAN DIEGO, CALIFORNIA; GREGORY J. SMITH, SAN DIEGO COUNTY ASSESSOR; and PAUL BOLAND, SAN DIEGO COUNTY TAX COLLECTOR,

Respondents.

Petition For Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

LLOYD M. HARMON, JR.,
County Counsel
County of San Diego
MIRIAM E. BREWSTER, Deputy
1600 Pacific Highway, Room 355
San Diego, California 92101-2469
(619) 531-4886
Counsel for Respondents

COCKLE LAW BRIEF PRINTING CO., (800) 225-6964
OR CALL COLLECT (402) 342-2831

BEST AVAILABLE COPY

QUESTIONS PRESENTED

1. Whether the use of federal property by a private research firm, to conduct research for profit in its own facilities, constitutes a taxable beneficial use of federal property.

2. Whether it is constitutional to calculate a state tax on the private beneficial use of federal property based on the value of the property.

TABLE OF CONTENTS

Page(s)

QUESTIONS PRESENTED i

TABLE OF CONTENTS ii

TABLE OF AUTHORITIES iii

OPINIONS BELOW 2

JURISDICTION 2

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED 3

STATEMENT OF THE CASE 3

I Factual Background 3

II Proceedings Below 4

SUMMARY OF ARGUMENT 7

REASONS FOR DENYING THE PETITION 7

I The Decision Is Consistent With The Long Line Of Federal Cases Which Hold That A Tax On The Private Beneficial Use Of Federal Property Is Constitutional 7

II The Decision Is Consistent With Previous Decisions Of This Court Which Hold That The Calculation Of A State Use May Be Based On The Value Of Federal Property 10

III The Issues Presented Are Not Of Broad Significance 13

CONCLUSION 14

TABLE OF AUTHORITIES

Page(s)

CASES

Jefferson County v. United States, 450 U.S. 901 (1981) 9

United States v. Anderson County, 761 F.2d 1169 (6th Cir. 1985) 10

United States v. City of Detroit, 355 U.S. 466 (1958) 11

United States v. Colorado, 627 F.2d 217 (10th Cir. 1980) 9, 10

United States v. Fresno, 429 U.S. 452 (1977) .. 11, 12, 13

United States v. New Mexico, 455 U.S. 720 (1982) .. *passim*

CONSTITUTIONAL PROVISIONS

U.S. Const., art. VI, clause 2 3

STATUTES

California Revenue and Taxation Code

Section 104 4

Section 105 4

Section 107 4

28 United States Code

Section 1254(1) 2

Section 1291 2

Section 1292(b) 2

Section 1331 2

Section 1345 2

No. 95-128

In The

Supreme Court of the United States

October Term, 1995

UNITED STATES OF AMERICA,

Petitioner,

v.

COUNTY OF SAN DIEGO, CALIFORNIA; GREGORY J. SMITH, SAN DIEGO COUNTY ASSESSOR; and PAUL BOLAND, SAN DIEGO COUNTY TAX COLLECTOR,

Respondents.

Petition For Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

TO THE HONORABLE SUPREME COURT:

Defendants/respondents County of San Diego, a political subdivision of the State of California, and its assessor and tax collector, submit this brief in opposition to the petition for a writ of certiorari submitted by plaintiff/petitioner United States of America.

OPINIONS BELOW

The decisions of the Ninth Circuit Court of Appeals (App., 1a-10a, 11a-26a) are reported at 965 F.2d 691 and 53 F.3d 965.[1] The opinions of the district court (App., 27a-44a, 45a-49a) are unreported.

JURISDICTION

The jurisdiction of this Court is invoked under 28 U.S.C. section 1254(1).

The jurisdiction of the Ninth Circuit Court of Appeals was invoked on the first occasion under 28 U.S.C. section 1292(b), as a permissive interlocutory appeal, and subsequently under 28 U.S.C. section 1291, as an appeal as a matter of right from a final order of the district court granting summary judgment in favor of the County of San Diego.

The jurisdiction of the District Court for the Southern District of California was invoked under 28 U.S.C. sections 1331 and 1345.

The County determined that the device is a real property improvement, which General Atomics uses to earn millions of dollars in profit and to acquire invaluable expertise.

---

[1] "App." refers to the Appendix to the United States' Petition for Certiorari.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The constitutional and statutory provisions involved are Article VI, Clause 2, of the United States Constitution and sections 104, 105, and 107 of the California Revenue and Taxation Code. App., 51a-52a.

STATEMENT OF THE CASE

The United States of America seeks a writ of certiorari to review a decision of the United States Court of Appeals for the Ninth Circuit, which affirmed the district court's grant of summary judgment to the County of San Diego. The United States' suit challenges the constitutionality of the California possessory interest tax which the County of San Diego imposes on a federal contractor, General Atomics.

I. Factual Background

General Atomics is a private research and development firm which conducts fusion research for profit. As part of its commercial enterprises, General Atomics designed and constructed a nuclear fusion "device" which it uses to conduct research under federal contracts. General Atomics earns millions of dollars in profit and gains marketable expertise from its use of the 400-500 ton device, which is a real property improvement to General Atomics' private facilities. App., 2a, 5a-7a, 13a, 18a-19a. California cannot impose a real property tax on the device because it is owned by the federal government. However, California does impose a possessory interest

tax on the private beneficial use of such real property improvements. Cal. Rev. & Tax. Code, §§ 104, 105, 107.

Consequently, the County of San Diego imposed a possessory interest tax on General Atomics' beneficial use of the device in its San Diego facilities.[2]

The possessory interest tax is calculated based on the value of the device, but the calculation takes into account the contractual restrictions on General Atomics' use of the device so that only the private use is taxed. Pet., 5 n.3.[3] General Atomics paid taxes of $568,002.12, including penalties and interest, for tax years 1978-81 and 1987-88. This amount was reimbursed by the federal government as provided by contract. General Atomics did not make payment on the remaining tax bills, which total $721,979.55 for tax years 1982-85 and 1989. App., 13a.

II. Proceedings Below

The United States commenced this action in 1989, seeking a declaratory judgment that (i) the possessory interest tax is imposed on federal property in violation of the federal constitution; (ii) General Atomics does not

---

[2] The County of San Diego has taxed General Atomics' use of two nuclear fusion devices. The first device operated from 1978 until 1984. The second device has remained in use since it was built in 1986. Since the County of San Diego taxed both devices in the same manner, no distinction has been made between the devices in this litigation. They are referred to collectively as the "device."

[3] "Pet." refers to the United States' Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

have a possessory interest under state law; and (iii) the methodology used to value the possessory interest is improper. CR 1.

The district court granted summary judgment in favor of the County of San Diego on the first two issues, finding that the tax was not imposed on federal property (the device) but on General Atomics' "beneficial use" of the device, which was taxable under state law. App., 27a-44a. The Court explained that the use of the device is beneficial not only because General Atomics receives large fees for its work with the device, but because "[General Atomics] gains and indeed sells . . . knowledge and expertise in fusion research" which allows General Atomics to market itself "to various customers, including the United States and foreign governments." App., 31a. The United States unsuccessfully moved for reconsideration of this decision, on the ground that the tax was imposed on General Atomics' "knowledge and expertise" rather than on General Atomics' use of the device. CR 38.

The United States then took an interlocutory appeal on the issue of whether General Atomics had a taxable possessory interest in the device. CR 58. In its decision affirming the district court's findings, the Ninth Circuit Court of Appeals agreed that General Atomics benefitted from use of the device by earning substantial profits and acquiring valuable expertise which it then markets. App., 18a-19a. The court concluded that "the County's taxation of this beneficial use is not a tax on federal property, but rather a tax on an 'essentially independent commercial enterprise.' " App., 19a.

On remand, the United States moved for leave to amend its complaint to allege that the tax discriminates against General Atomics because no other contractor is taxed for "acquiring expertise." CR 68. The district court denied this motion. The County subsequently moved for summary judgment on the remaining issue, i.e., whether the methodology employed to value the possessory interest was erroneous. CR 95. This issue presented a question of state law, on which the United States could not proceed because it failed to first exhaust state administrative remedies. The United States opposed the motion, arguing that the issue of valuation presented a constitutional question because the tax exceeded the value of General Atomics "knowledge" and thus was necessarily imposed on federal property. CR 88. Rejecting this argument, the district court granted the County of San Diego's motion and entered judgment in favor of the County.

On appeal of the final judgment, the Ninth Circuit Court of Appeals affirmed the district court's findings on all issues. The court of appeals rejected the contention that the tax is imposed on "knowledge," stating that "even though the possessory interest is valuable because of the fee and experience General Atomics reaps, the tax is based on the possessory interest itself. . . . " App., 8a. The court of appeals also rejected the contention that the valuation methodology presented a constitutional issue, concluding that "[i]t is not unconstitutional for the County to calculate the value of General Atomics' possessory interest by turning to the value of the device." App., 9a.

SUMMARY OF ARGUMENT

The United States fails to present a basis for review of the Ninth Circuit's decision. The decision does not narrow federal tax immunity, or depart from earlier decisions, as the United States contends. The decision is consistent with existing federal law, because the possessory interest tax is imposed on General Atomics' private beneficial use of the device rather than on General Atomics' "acquisition of knowledge." Federal courts have long recognized that the states may tax the private beneficial use of federal property, and that the tax may be based on the value of the property being used.

REASONS FOR DENYING THE PETITION

I. The Decision Is Consistent With the Long Line Of Federal Cases Which Hold That A Tax On The Private Beneficial Use Of Federal Property Is Constitutional.

The United States mistakenly asserts that the Ninth Circuit's decision narrows federal tax immunity and "departs from earlier federal decisions." Pet., 13-14. On the contrary, the decision is consistent with the long line of federal cases which hold that a tax on the private beneficial use of federal property is constitutional. See, *United States v. New Mexico*, 455 U.S. 720 (1982).

In *New Mexico*, this Court was asked to decide whether a state may tax federal contractors for using federal property in performing management and other contract services at federally-owned atomic laboratories. Starting with the underlying constitutional principle that

a state may not tax the United States directly, the Court stated that "the limits on the immunity doctrine are, for present purposes, as significant as the rule itself." Id. at 734. After reviewing its earlier decisions, the Court explained that "where a use tax is involved, immunity cannot be conferred" on a contractor even if the contractor uses federal property to provide goods or services to the federal government. Id. "In such a situation the contractor's use of the property 'in connection with commercial activities carried on for profit' is 'a separate and distinct taxable activity.' " Id. at 734-35. The Court concluded that its decisions left room for tax immunity "in only one circumstance: when the levy falls directly on the United States itself, or on an agency or instrumentality so closely connected" that the two cannot be viewed as separate entities. Id. at 735.

General Atomics' use of the device is taxable under these principles, because General Atomics is not an agent of the United States, and it undeniably uses the device "in connection with commercial activities carried on for profit." Id. at 734-35. General Atomics is in the business of conducting research for profit, and it earns millions in profit every year from using the device under its contracts with the federal government. App., 13a. General Atomics also gains expertise and a reputation which make it highly marketable in the field of fusion technology. In fact, during the period relevant to this litigation, 1980 through 1989, the Fusion Division of General Atomics received contract revenues of nearly one-half billion dollars. CR 38. (Overskei decl. at p. 3.) This figure includes $351,645,100.00 received under the contracts covering the use of the device, $68,573,100.00 received

under other federal contracts, and $24,323,900.00 received from commercial firms. CR 38. (Overskei decl. at p. 3.)

There is no doubt that the use of the device has been a key factor in the success of General Atomics' fusion program. In its advertisements, General Atomics refers to the device as the "heart" of its fusion program, which it describes as "on the cutting edge" of fusion technology. CR 22. (exh. to Overskei Depo.) Such beneficial use of federal property is clearly taxable under the principles set forth in *New Mexico.* As this Court held in *New Mexico,* the reimbursement of expenses, payment of a profit, and the acquisition of expertise are all evidence of a taxable beneficial use. 455 U.S. at 723-724 and n.3.

The United States asserts that General Atomics' use of the device is not beneficial because General Atomics "merely manages" the device. Citing *United States v. Colorado,* 627 F.2d 217 (10th Cir. 1980), aff'd sub nom. *Jefferson County v. United States,* 450 U.S. 901 (1981), the United States argues that under federal law, a "tax that is assessed on a contractor who merely manages federal property" is an unconstitutional tax on federal property. Pet., 16. The United States' argument fails because *Colorado* does not invalidate a use tax because the federal contractor "merely managed" federal property. *Colorado* invalidates the tax because the tax statute assessed users of federal real property "as though the [users] were the *owner[s]* of such property." 627 F.2d at 218; emphasis added. The Court found that the tax was not imposed on the contractor's "use" of the property, because the use was limited by contract. Id. This Court concluded a tax "under the provisions of [this state tax statute], is in reality a tax on the property itself. . . . " Id.

Colorado does not apply here, because General Atomics is not taxed on the entire value of the device. General Atomics is taxed only on its possessory interest in the device, an interest which is substantially less than the value of the device itself. In fact, the tax has varied from year to year based on General Atomics' use of the device, and it was not imposed at all in the year the device was not operational. CR 1 at 9-10. Since the tax falls only on General Atomics' use of the device, the tax does not suffer from the same constitutional infirmity as the statute in *Colorado*. App., 15a-16a.[4]

II. The Decision Is Consistent With Previous Decisions Of This Court Which Hold That The Calculation Of A State Use Tax May Be Based On The Value Of Federal Property.

The United States also argues that, if General Atomics has a beneficial use of the device at all, General Atomics has "benefitted" by using the device in only one instance, i.e., in the receipt of consulting fees amounting to $176,000.00. The United States therefore concludes that the possessory interest tax is excessive because the tax exceeds the amount of the "benefit." Pet., 20-21.

---

[4] The United States also relies on *United States v. Anderson County*, 761 F.2d 1169 (6th Cir. 1985), for the proposition that a federal contractor who manages federal property cannot have a separate taxable interest in the property. Pet., 17-18 n.9. *Anderson County* does not stand for this proposition. *Anderson County* invalidates a state tax because the state supreme court had already determined that the contractor did not possess a taxable interest under state law. 761 F.2d at 1172-75.

This argument makes no sense, because the tax is imposed on the use of the device, not on the fees received. The receipt of the fees is merely evidence that a beneficial use exists. Moreover, the United States seriously mischaracterizes the true extent of General Atomics' beneficial use. While General Atomics receives fees for related work, it also benefits from using the device under federal contract – earning nearly $352 million for its work with the device between 1980 and 1989, including $2.5 million per year in profit. CR 38. (Overskei decl. at p. 3.) In addition to these contract fees, General Atomics has gained invaluable experience which it markets to obtain other federal and private contracts for fusion-related research or technologies. CR 38. (Overskei decl. at p. 3.)

The possessory interest tax on this beneficial use is not "constitutionally flawed" because it is based on the value of the device, as the United States argues. This Court held long ago that a state use tax may be based on the value of the federal property being used. *United States v. City of Detroit*, 355 U.S. 466, 470 (1958). In *Detroit*, the federal government argued that a state use tax which is measured by the value of federal property "should be treated as nothing more than a contrivance to lay a tax on that property." Id. This Court rejected this argument, stating that "[a] tax for beneficial use of property, as distinguished from a tax on the property itself, has long been a commonplace in this Country. [ ] In measuring such a use tax it seems neither irregular nor extravagant to resort to the value of the property used. . . . " Id.

This principle was discussed again in *United States v. Fresno*, 429 U.S. 452, 462, n.10 (1977), a case which upheld

the imposition of the very tax at issue here, California's possessory interest tax. Id. at 455-456. In *Fresno*, the possessory interest tax was applied to federal employees who lived in government housing and the tax was calculated based on the value of the homes. Id. at 456. Noting that a use tax may be measured by the value of the federal property being used, the Court stated "[a]ppellee counties have sought to tax only the individual appellants' interests in the [housing] and have reduced their assessments to take account of the limitations on the use of the houses imposed by the Government." 429 U.S. at 462 n.10.

The tax assessments here are constitutional because they are computed in the same manner as the assessment in *Fresno*. The assessments against General Atomics are based on the value of the federal property being used, but take into account the limitations on the use of the device. App., 9a, CR 89. As the United States states in its petition for certiorari, the tax assessor calculates the value of the possessory interest by determining the cost of the property being used, the average life and salvage value of the property, the duration and extent of the taxpayer's right to use the property, any reversionary interest, and the appropriate allowance for depreciation. Pet., 5 n.3. The United States' own expert on valuation explained that the County of San Diego applied a "usage factor" to calculate General Atomics' interest in the device each year. CR 89. The expert testified that a usage factor of 30% was applied in tax year 1978-79, the only tax year for which the expert provided a figure. CR 89. (Steel decl., at pp. 2-3.)

Such a method of calculating the possessory interest tax is constitutional under well settled law. App., 9a. Consequently, there is no need to revisit this issue.

III. The Issues Presented Are Not Of Broad Significance.

The questions presented to this Court by the United States simply are not of "broad significance" because the body of federal law governing tax immunity is well-established, and the United States presents no new issues. While the United States argues that billions of dollars in federal property is in private hands and "[a]n annual tax on even a portion of the value of this property . . . would meaningfully disturb 'the absolute federal immunity from state taxation' " (Pet., 24), federal law is settled on this point as well.

A tax is not unconstitutional because it imposes an "economic burden on a federal function" by taxing those who "deal with the federal Government." *Fresno*, supra, 429 U.S. at 462. Nor is tax immunity conferred on federal contractors because the tax is paid with federal funds. *New Mexico*, supra, 455 U.S. at 735. In *New Mexico*, this Court explained the immunity principles derived from its earlier decisions:

> "If the immunity of federal contractors is to be expanded beyond its narrow constitutional limits, it is Congress that must take responsibility for the decision, by so expressly providing. . . . Absent congressional action, we have emphasized that the States' power to tax can be denied only under 'the clearest constitutional mandate.' [ ]" Id. at 737-38.

Since there is no constitutional prohibition against the tax involved here, and since Congress has not acted to extend federal tax immunity to General Atomics, the tax is permissible under settled principles of federal law.

While the United States complains of the burden of state taxation, it voluntarily assumed the tax burden here, when it agreed to reimburse General Atomics for the possessory interest taxes. Furthermore, while the United States implies that such state taxation is a great burden on the federal government, the burden may not be nearly as significant as the United States implies. The taxes imposed on General Atomics for tax years 1980 through 1989, including penalties and interest, total only $1.3 million. This is less than one-half of one percent of the $352 million in contract payments made to General Atomics during the same time period.

CONCLUSION

For the reasons set forth above, the Petition for Writ of Certiorari should be denied.

Respectfully submitted,

LLOYD M. HARMON, JR.,
County Counsel
County of San Diego
MIRIAM E. BREWSTER, Deputy
1600 Pacific Highway, Room 355
San Diego, California 92101-2469
(619) 531-4886
Counsel for Respondents